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IN THE
Supreme Court of the United States
OCTOBER TERM, 1994

BENJAMIN B. ALARID, *ET AL.*,
Petitioners,

v.

SECRETARY OF THE NEW MEXICO DEPARTMENT OF TAXATION AND REVENUE,
Respondent.

On Petition for Writ of Certiorari to the New Mexico Court of Appeals

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BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether intergovernmental immunity exists between individual states, making it unconstitutional for New Mexico to tax retirement income paid to New Mexico residents by the State of California while exempting from tax retirement income paid to New Mexico residents by the State of New Mexico.

2. Whether a New Mexico tax exemption applicable to retirement income from New Mexico state educational institutions, but not to retirement income from California state educational institutions, discriminated against the federal government in violation of the doctrine of intergovernmental immunity where the federal government funded the retirement benefits paid by both states pursuant to federal contracts with each state's respective educational institutions.

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BRIEF IN OPPOSITION

The Secretary of the New Mexico Department of Taxation and Revenue respectfully requests that this Court deny the Petition for Writ of Certiorari filed by Benjamin B. Alarid, *et al*.

STATEMENT OF THE CASE

For calendar years 1986, 1987, 1988 and 1989, the State of New Mexico exempted from income tax retirement income paid to former employees by New Mexico's state educational institutions. NMSA 1978, Section 22-11-42(A) (1989 Repl.

Pamp.). During this four-year period, the retirement income paid to New Mexico residents formerly employed by other states' educational institutions, as well as private educational institutions, was subject to tax. The exemption afforded by Section 22-11-42 was repealed effective January 1, 1990. Laws 1990, ch. 49, §§ 17, 24.

Petitioners are New Mexico residents formerly employed by the University of California.[1] Between 1986 and 1989, petitioners received retirement income from the State of California that was subject to New Mexico income tax. Findings of Fact ¶¶ 8-11, App. F at 29-30. Petitioners' retirement income constituted deferred compensation for work performed at Los Alamos, New Mexico, for the University of California under contracts between the State of California and the United States Department of Energy. Finding of Fact ¶ 8, App. F at 29.

During the same four-year period, New Mexico residents formerly employed by New Mexico educational institutions received retirement income from the State of New Mexico that was not subject to state income tax. Findings of Fact ¶¶ 12-14, App. F at 30-31. At least some of this retirement income constituted deferred compensation for work performed for New Mexico universities under contracts between the State of New

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[1] See stipulated Finding of Fact ¶ 1, adopted by the trial court below and set forth in Appendix F to the Petition for Writ of Certiorari at pages App. 27-32. Hereinafter, references to the Findings of Fact will be accompanied by a page reference to Appendix F.

Mexico and the federal government. Finding of Fact ¶ 13, App. F at 30.

The federal contracts held by both the State of California and the State of New Mexico provided for federal funding of each state's retirement obligation to its employees. Findings of Fact ¶¶ 6, 8, 12, 13, App. F at 28-31. The parties to this case stipulated that for purposes of the New Mexico Income Tax Act, the only material difference between the retirement income of petitioners and the retirement income of retirees of New Mexico educational institutions was that the ultimate source of petitioners' retirement income was the State of California, rather than the State of New Mexico. Finding of Fact ¶ 15, App. F at 31.

REASONS FOR DENYING THE WRIT

I. Intergovernmental Tax Immunity Does Not Apply Between Sovereign States.

Petitioners urge this Court to accept certiorari based on their assertion that New Mexico is the only state to hold that intergovernmental tax immunity ("ITI") does not apply between sovereign states. Petition at 12. In fact, only two months ago this Court denied review of a virtually identical decision by the State of Oregon. *Simpson v. Department of*

Revenue, 318 Or. 579, 870 P.2d 824, *cert. denied*, 115 S.Ct. 189 (1994).[2]

In *Simpson* the Oregon Supreme Court affirmed the ruling of its tax court that the retirement income of a former employee of the State of Alaska was subject to income tax in Oregon, notwithstanding the fact that Oregon exempted from tax the retirement income of its own state employees. The tax court specifically rejected plaintiffs' argument that the ITI doctrine, as set out in *Davis v. Michigan*, 489 U.S. 803 (1989), applied to the relationship between individual states. The tax court first noted that the plaintiffs in *Davis* were subject to two sovereigns: the State of Michigan and the federal government. In contrast, the plaintiffs in *Simpson* were Oregon residents "not subject to the sovereign powers of Alaska... While one state cannot impose a tax or burden on another, it may impose a tax on its own residents' income received from another state." 12 Or. Tax 455 (1993).

Far from breaking new ground, the decision of the New Mexico Court of Appeals in this case relies on the same reasoning employed by Oregon in *Simpson*, and by the

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[2] The Petition for Writ of Certiorari filed in this Court on July 5, 1994 presented the following question: "Is it constitutionally permissible under principles of intergovernmental tax immunity as set forth in *Davis v. Michigan Department of Treasury*, 489 U.S. 803, 57 LW 4389 (1989), for Oregon to enact tax on public retiree benefits paid by other states, and to exempt from such tax its own public retiree benefits, when effect is reduction in Oregon's employment costs and simultaneous reduction in revenue collected by federal treasury?" Review was denied October 3, 1994.

supreme courts of Louisiana, Minnesota and Kansas in earlier cases upholding tax exemptions each state enacted in its own favor but did not extend to sister states.[3] The basis for these decisions lies in the limited nature of state sovereignty, as opposed to the more encompassing sovereignty of the federal government. As had the Oregon court in *Simpson*, the New Mexico Court of Appeals distinguished application of the ITI doctrine in *Davis*; unlike the federal government, whose sovereignty overlaps that of all of the states, neither California nor New Mexico has the ability to affect the other's governmental functions "by reaching out to tax those functions" in the other state. Absent the need for one sovereign to protect itself from the taxing power of another, "there is no basis on which to apply the ITI doctrine." App. B at 19-20.

The New Mexico court also distinguished application of the ITI doctrine in *Pledger v. Bosnick*, 306 Ark. 45, 811 S.W.2d 286 (1991), *cert. denied* 113 S.Ct. 3034 (1993), the sole case supporting petitioners' position. The court noted that the Arkansas Supreme Court relied on two cases that "dealt only with the application of the ITI doctrine to overlapping sovereigns and did not apply the ITI doctrine to taxation of one state by another state. We see no other analysis in *Pledger*

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[3] *Warren County, Mississippi v. Hester*, 54 So.2d 12 (La. 1951); *Minnesota v. City of Hudson*, 42 N.W.2d 546 (Minn. 1950); and *Kansas v. Holcomb*, 116 P. 251 (Kan. 1911), discussed *infra* at pages 7-8.

which supports application of the ITI doctrine in this context."[4] App. B at 21.

Although this Court has not addressed the application of the ITI doctrine between states, it has ruled on the underlying issue of state sovereignty, holding that a state's sovereignty does not extend into the territory of any other state, but is wholly contained within its own borders. In *Nevada v. Hall*, 440 U.S. 410 (1979), the Court found that nothing in the Constitution prohibited the State of California from asserting jurisdiction over the State of Nevada in a tort action filed in California.[5] Although earlier cases presumed that states intend to adopt policies of broad comity toward one another, "this presumption reflected an understanding of state policy, rather than a constitutional command." *Id.* at 426.

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[4] In *Pledger*, plaintiffs comprised three groups of Arkansas residents retired from employment with (1) various United States civil service agencies; (2) various branches of the United States armed services; and (3) agencies and political subdivisions of other states. Without differentiating among these groups, the state court found that the exemption granted to Arkansas state retirees unconstitutionally discriminated against retirees of both the federal government and other states. With the exception of a general reference to *Davis v. Michigan*, 489 U.S. 803 (1989), which dealt only with *federal* retirees, the opinion contains no analysis and no authority in support of its finding that the ITI doctrine applies between states.

[5] The issue arose from a $1 million jury verdict in favor of California residents who filed a tort action against Nevada following an automobile accident on a California highway with a Nevada-owned vehicle.

In *Georgia v. Chattanooga*, 264 U.S. 472 (1924), the Court refused to enjoin condemnation of real property owned by Georgia in the state of Tennessee, finding that "[l]and acquired by one state in another state is held subject to the laws of the latter and to all the incidents of private ownership.... *The sovereignty of Georgia was not extended into Tennessee.*" 264 U.S. at 480-481 (emphasis added). And in an early case dealing with state taxes, the Court held that Maryland was entitled to impose a tax on New York and Pennsylvania bonds held by a Maryland resident, even though the bonds would be exempt from tax in the issuing state: "We know of no provision of the Constitution of the United States which prohibits such taxation.... One State cannot exempt property from taxation in another. Each State is independent of all the others in this particular." *Bonaparte v. Tax Court*, 104 U.S. 592, 594 (1881).

Similarly, the highest courts of at least three states have upheld discriminatory tax exemptions favoring the enacting state over all other states. Each decision was based on the finding that a state acting outside its borders takes the status of a private citizen and cannot assert the privilege of sovereignty. The first case, *Kansas v. Holcomb*, 116 P. 251 (Kan. 1911), denied a Kansas property tax exemption to a Missouri public waterworks plant located just across the Kansas border. The Kansas Supreme Court rejected Missouri's attempt to claim the same tax exemption that Kansas granted to its own public property, holding that when another state comes into Kansas "it comes as a private party and brings with it none of the prerogatives of sovereignty." 116 P. at 254.

Forty years later, the Louisiana Supreme Court held that a provision of the Louisiana constitution exempting all public property from taxation did not apply to a Mississippi-owned bridge that extended into Louisiana. *Warren County, Mississippi v. Hester*, 54 So.2d 12 (La. 1951). Under similar facts, the Minnesota Supreme Court held that the City of Hudson, Wisconsin, could not claim the tax exemption which Minnesota granted to the property of its own municipalities. *Minnesota v. City of Hudson*, 42 N.W.2d 546 (Minn. 1950).

The federal and state cases discussed above effectively dispose of the issue in this case. There is nothing startling or new in the New Mexico Court of Appeals' conclusion that California is not entitled to claim intergovernmental immunity from taxation in New Mexico. As first discussed by Justice Marshall in *M'Culloch v. Maryland*, 17 U.S. 316 (1819), the ITI doctrine applies to maintain the balance between two sovereigns who share overlapping jurisdiction over the same territory. The concern underlying the ITI doctrine is clear:

> If the states may tax one instrument employed by the government, in the execution of its powers, they may tax any and every other instrument. They may tax the mail; they may tax the mint; they may tax patent rights; they may tax the papers of the custom house; they may tax judicial process; they may tax all the means employed by the government, to an excess which would defeat all ends of government.

17 U.S. at 432.[6] In this case, the ITI doctrine does not apply between California and New Mexico because California, unlike the federal government, does not enjoy the status of sovereign within the State of New Mexico. Nor does California have the status of sovereign with regard to petitioners, all of whom are residents of New Mexico. To suggest that New Mexico is capable, through an income tax levied on its own residents, to defeat "all the ends of government" of the State of California is patently absurd. As a long line of case law already holds: when one state moves into the territory of another, "it comes as a private party and brings with it none of the prerogatives of sovereignty." *Holcomb*, *supra*, 116 P. at 254. As a private party, California has no right to claim immunity from the tax laws of its sister state.

II. The New Mexico Tax Did Not Discriminate Against Petitioners Based on Their Dealings With the Federal Government.

Petitioners' second reason for seeking this Court's review is their contention that the New Mexico Court of Appeals "confuses" the legal incidence principle (states can't tax the

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[6] In *Collector v. Day*, 78 U.S. 113 (1870), the Court invoked the ITI doctrine to prohibit federal taxation that directly affected a traditional state function. The Court held that the states' power of taxation was not abridged by the grant of a similar power to the federal government, but was to be concurrently exercised by the two governments. *Day* extended the ITI doctrine to prevent the federal government from exercising this *concurrent* taxing power in a manner which would prevent the states from performing their traditional governmental functions.

federal government) and the nondiscrimination principle (states can't tax so as to discriminate against the federal government) of the ITI doctrine. Petition at 13. In fact, the court of appeals separately considered each of these principles, concluding: "*not only* did the New Mexico tax not fall on the United States, *but also the tax did not discriminate against Plaintiffs based on their dealings with the federal government.*" App. B at 13 (emphasis added).

Petitioners argue that the legal incidence analysis was improper because a state tax that discriminates against the federal government violates the ITI doctrine "notwithstanding the fact that the legal incidence of the tax does not fall upon the government itself." Petition at 14. Respondent does not disagree. In this case, however, the court of appeals' analysis of the legal incidence principle was made in conjunction with its conclusion that the New Mexico tax *did not discriminate* against the federal government. The fact that the court of appeals undertook to analyze both the nondiscrimination *and* the legal incidence aspects of the ITI doctrine was not improper and does not indicate "confusion." Indeed, the court would have been remiss had it examined only one of the two bases on which a tax could be held to violate the ITI doctrine.

What the court of appeals clearly understood, and what petitioners have consistently failed to grasp, is that a discriminatory tax does not, in itself, violate the ITI doctrine. It is only when the basis for the discrimination is the taxpayer's relationship with the federal government that the doctrine is implicated. Petitioners are incorrect in stating that the

"controlling factor" in *Davis v. Michigan*, *supra*, was the economic burden of the tax. *See*, Petition at 15. The portion of the *Davis* opinion petitioners cite in support of this position is taken from a footnote written in response to Justice Stevens' dissent. The "controlling factor" of the *Davis* decision was that the Michigan income tax discriminated against federal retirees "on account of their dealings" with the federal government.[7] 489 U.S. at 814.

In the instant case, the court of appeals recognized that in *Davis* "the only difference between the two classes of taxpayers was the source of their income. Employees whose retirement income was received from the State of Michigan were exempt from taxation, while employees whose retirement income was received from the federal government were not exempt." App. B at 14. As the court further noted, petitioners in this case stipulated that the source of their retirement income was the State of California, not the federal government. *Id.* *See also*, Finding of Fact ¶ 15, App. F at

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[7] Each state tax case relied upon by petitioners, including *Davis*, involved a tax imposed on every member of a class of persons dealing directly with the federal government. *See*, *Memphis Bank & Trust v. Garner*, 489 U.S. 390 (1983) (holders of federal obligations); *Washington v. United States*, 460 U.S. 536 (1983) (federal contractors); *United States v. County of Fresno*, 429 U.S. 452 (1977) (federal employees living in federally-owned housing); *Phillips Chemical Co. v. Dumas Independent School District*, 361 U.S. 376 (1960) (lessees of federally-owned real property). Because petitioners in this case were dealing with the State of California and not the federal government, the court of appeals did not err in holding that the exemption afforded to New Mexico retirees did not discriminate against petitioners *on account of their dealings* with the federal government.

31. Despite this admission, petitioners insist that the tax on their retirement benefits discriminated against the federal government because the government funded those benefits under the terms of its contract with the State of California. Petitioners overlook the fact that the retirement income of employees of New Mexico universities also was funded by the federal government under the terms of contracts held with the State of New Mexico, and yet that income was exempt from tax. Findings of Fact ¶¶ 12, 13, App. F at 30.

Common sense and elementary logic dictate that a tax imposed on California retirement income funded by the federal government, but not imposed on New Mexico retirement income funded by the federal government, does not discriminate against the federal government.[8] In this case, it was the identity of the payor (State of California versus State of New Mexico) that was the determinate factor. To the extent the New Mexico income tax discriminated, it discriminated against the State of California. As the New Mexico Court of Appeals correctly found: "The discriminatory impact of which [petitioners] complain is therefore not directed toward the federal government and is not prohibited." App. B at 17.

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[8] To argue otherwise is equivalent to arguing that New Mexico's income tax exemption for blind taxpayers discriminates against the federal government. Presumably, some federal employees are blind and receive the exemption; other federal employees are not blind and do not receive the exemption. According to petitioners' reasoning, this discriminates against the federal government. Such reasoning is clearly erroneous. The exemption "discriminates" against sighted taxpayers—it does not discriminate against the federal government.

CONCLUSION

For the reasons stated above, the Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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